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25 October 2017

Insurance in Superannuation Working Group
Project Management Office
ISWG-PMO@kpmg.com.au

Dear Sir/Madam,

Consultation Paper: *Insurance in Superannuation Code of Practice*

The Association of Superannuation Funds of Australia (ASFA) is pleased to provide this submission in response to the Consultation Paper: *Insurance in Superannuation Code of Practice*.

About ASFA

ASFA is a non-profit, non-political national organisation whose mission is to continuously improve the superannuation system, so all Australians can enjoy a comfortable and dignified retirement. We focus on the issues that affect the entire Australian superannuation system and its \$2.3 trillion in retirement savings. Our membership is across all parts of the industry, including corporate, public sector, industry and retail superannuation funds, and associated service providers, representing over 90 per cent of the 14.8 million Australians with superannuation.

We would like to thank you for the opportunity to provide feedback on the draft Code and would be happy to discuss our comments.

Should you have any questions on any of the matters raised in this submission please do not hesitate to contact me on (02) 8079 0849 or kwhitton@superannuation.asn.au or Byron Addison on (02) 8079 0834 or baddison@superannuation.asn.au.

Yours sincerely

Ken Whitton
Senior Policy Advisor

General observation

ASFA has consulted its members and the following submission relates to the areas of most interest in the Code that ASFA members have identified. The Code is a positive initiative and provides a rigorous and ambitious framework for trustees. We recognise all of the hard work, consultation and cooperation by participants over the last 12 months and the release of this draft Code is a significant industry achievement.

In general, ASFA considers that the Code is a great first step and provides a solid foundation for ongoing improvements in the way insurance is delivered to superannuation fund members. The Code will be a living document and will be able to evolve over time in response changing circumstances. At the same time we acknowledge that a degree of flexibility is required in applying the Code to allow trustees to meet the changing needs of their members within current obligations.

Summary of key comments

- The draft Code needs to more clearly define the concept of Automatic Insurance Member (AIM) and outline more precisely transition arrangements for trustees.
- It is important that the Code contain benefit design premium limit tests for automatic insurance to ensure that retirement savings are not being unnecessarily eroded.
- An insurance cessation provision commencing with a 13 month period of no contributions being received is a sensible first step.
- ASFA expects that broader industry and government efforts to manage duplicate superannuation account issues will continue to assist with unnecessary duplicate insurance.
- ASFA sees potential for the insurance definitions to be brought into alignment with the SIS conditions of release although this would require legislative change.
- The claims handling measures in the draft Code will go a long way towards improving claimant experience however ASFA contends that trustees should be provided with greater flexibility to extend the 15 day period to review declined claims.
- ASFA supports the flagging of vulnerable members but only where the member approves such a record being kept.
- In order for funds to retain an opportunity to establish premium adjustment arrangements ASFA supports the proposed transparency and prescribed use of funds measures.
- More work needs to be done by the ISWG to codify premium refund protocols, particularly in relation to duplicate income protection claims.
- ASFA agrees that trustees should bind its third party providers, including insurers and administrators, to obligations of the Code through contractual arrangements over time.
- ASFA considers that trustees will need a degree of flexibility in complying with the Code and supports consideration being given to compliance on an “if not why not” basis.
- ASFA considers that of the available options self-regulation is the best in the short term and that other enforcement options can be explored later once there is a track record by which the success of the Code can be judged.

Key comments in detail

A. Scope of the Code

The draft Code needs to more clearly define the concept of Automatic Insurance Member (AIM) and outline more precisely transition arrangements for trustees.

ASFA considers that the current definition for Automatic Insurance Members (AIMs) referred to for the first time in this section is inconclusive. Currently it states that insurance issued under an automatic acceptance limit determines AIM status, however, it later advises that if a member either applies for, or varies cover, they are not regarded as an AIM.

We understand that it is common across the industry for funds to offer a range of additional insurance benefits at the time of commencement of membership under an automatic acceptance limit requiring only a very light form of application or variation on the part of the member. In these cases, it is our view that the greater protections afforded to AIMs should be maintained for those individuals. On later occasions, should individuals change their cover or apply for additional insurance benefits we are comfortable with them being removed from the AIM group.

Some ASFA members are concerned about the transition arrangements, in particular the effect of 3.10 which states that the “benefit design and premium limit standards in Section 4 apply to any new or updated policies after the date we adopt this Code”. ASFA considers that there needs to be a materiality threshold for any update made in the transition period so that minor revisions or changes to the terms and conditions of existing policies don’t trigger the application of the Code and all the attendant system changes required for a new benefit design.

For ASFA’s comments on matters relating to Code governance refer to section I of this paper.

B. Appropriate and affordable cover

It is important that the Code contain benefit design premium limit tests for automatic insurance to ensure that retirement savings are not being unnecessarily eroded.

An insurance cessation provision commencing with a 13 month period of no contributions being received is a sensible first step.

ASFA expects that broader industry and government efforts to manage duplicate superannuation account issues will continue to assist with unnecessary duplicate insurance.

1. Maximum premium limits based on % of earnings

ASFA supports the Code including the proposed % of Ordinary Time Earnings (OTE) from employment design tests, broadly described as:

A 1% design test - premiums for automatic cover will be set at a level that does not exceed 1% of OTE.

A 0.5% design test - premiums for automatic cover for members that are under the age of 25 will be set at a level that does not exceed 0.5% of OTE.

In our view it is important these tests are based on OTE from employment as opposed to the alternative of superannuation guarantee (SG) contributions as the Code is intended to be consumer oriented in its presentation. A lower % of an individual's OTE (salary) is much more likely to be understood and accepted by fund members over a higher % of an unknown (in many cases) contributions amount. Furthermore, it is OTE from which an employer's SG contribution obligation arises and with SG scheduled to rise, it would be unwise for industry to establish a test that increases premium limits in the medium term.

In consultation with ASFA members it has become apparent that clearer guidance on the application of these tests is required. Furthermore, funds should be afforded the flexibility to use representative samples of their membership and/or other reasonable proxies as determined by the trustees.

ASFA expects the Good Practice Guidance that is being prepared should deal with these matters although consideration should also be given to changing the current wording in the draft Code to avoid potential misunderstanding in relation to the test potentially applying to relevant segments of the membership and the membership generally. Replacing "and" with "or", in section 4.8 line 3 between the words "membership" and "for" may suffice to correct this.

ASFA members have also found the references in 4.8 to "automatic cover" and "Automatic Insurance Members" confusing and we consider the second reference should be amended to "members under the age of 25 with automatic cover" for consistency.

We also support funds being able to exceed these limits when it can be shown that the cover being provided is appropriate and reasonable to the particular membership, either partly or in whole. The current wording at 4.10, referencing "higher risk members" may be too prescriptive to allow this. A re-wording to the effect of allowing caps to be exceeded "where cover is appropriate and reasonable to the particular demographic" may be warranted.

2. Cessation of cover after 13 months without contributions (inactive accounts)

Introducing the cessation of cover for inactive accounts at the 13 month point is a sensible first step for this measure in the view of ASFA. We accept that there are reasonable arguments for either a shorter or longer duration of inactivity; however, to balance the erosive effects of insurance premiums with individuals maintaining insurance cover of value to them, 13 months is the most appropriate time limit at this point of time.

To inform this view we have considered a number of factors, including but not limited to:

- the state of administration capability across the industry;
- the current numbers of individuals with duplicate accounts and insurance;
- underinsurance levels in Australia;
- risks for insurance loss by individuals having breaks in employment;
- SG coverage and non-compliance of SG payments by employers; and
- ATO provisions relating to lost and un-contactable members.

We are open to this being reduced to a shorter period in the future if/when the specific issues relating to parents having breaks from work due to family commitments are addressed and new fund contributions reporting arrangements are operational from late 2018. There also needs to be a detailed consideration of the impact of further reductions to insurance coverage across the population before the cessation period is shortened.

ASFA also supports the associated communication protocols relating to this measure and agrees that funds should be able to alert individuals to the risks of cover ceasing in those communications. Similarly, should a fund member elect to retain insurance cover during a period of inactivity, that individual should not have to be exposed to the cessation mechanism again in the future at that fund.

3. Managing duplicate insurance

ASFA expects that the insurance cessation measure discussed above will have a significant impact on managing the issues related to duplicate insurance (as a result of duplicate superannuation accounts). It also needs to be remembered that this issue is greatest for those who may have duplicate superannuation accounts with multiple income protection accounts.

ASFA members overwhelmingly support the range of proposals in the draft Code and earlier ISWG discussion papers relating to the need for a combination of industry and regulator changes to assist with funds and individuals having greater visibility of insurance to prevent unwanted duplicate insurance. For example, ASFA considers that legislative and regulatory adjustment is required to assist with avoiding the issuance of unnecessary insurance. Initiatives in the future could include some existing SuperStream fields that are currently optional being made mandatory for employers to complete and funds should be able, with a member's permission, to search for existing insurances that an individual may already have.

C. Insurance Definitions

ASFA sees potential for the insurance definitions to be brought into alignment with the SIS conditions of release although this would require legislative change.

1. Scope to standardise definitions and/or align to SIS conditions of release

ASFA acknowledges that insurance definitions, and in particular definitions of disability, is a complex area and that there is a great variety of ways to define disability. Simplification could reduce access to benefits and have other unintended consequences in certain occupations or member categories. On the other hand members would greatly benefit from a definition that was simple and which made different policies easier to compare.

ASFA believes that the best first step in bringing the various definitions together is to align insurance definitions with SIS conditions of release. There are currently inconsistencies between certain disability and terminal illness definitions and the conditions of release which can mean that insurance benefits are payable but cannot be released or a condition of release is met but the insured benefit is not payable.

Alignment would require an amendment to the SIS legislation and regulations and any move to align industry definitions with the SIS conditions of release should involve significant consultation with the industry and insurers. It is likely that this would also help promote an increasingly standardised approach to definitions more broadly.

2. Further legislative change

As part of any review of existing legislation there is an opportunity to explore changes to the minimum insurance requirements for MySuper products including giving trustees discretion to offer whatever range of insurance benefits they feel are appropriate to their members. For example, income protection and/or rehabilitation payments in lieu of lump sum benefits, rather than the current arrangement where lump sum benefits are mandatory in legislation with income protection an optional addition. This would allow trustees greater freedom to provide insurance adapted to the needs of their particular membership and lower costs.

D. Claims handling

The claims handling measures in the draft Code will go a long way towards improving claimant experience however ASFA contends that trustees should be provided with greater flexibility to extend the 15 day period to review declined claims.

We recommend that the requirement for trustees to “review” the insurer’s decision in 6.22 be defined more clearly as it currently leaves the meaning of review open to various interpretations. It is our understanding that the purpose of the review is to make it clear that the trustee is ultimately responsible for the decision and that it needs to ensure that any decision made by its third-party insurer is rigorous and well-founded. Accordingly 6.22 should be amended to reflect this and make it clear that the degree of review is dependent on the specifics of each claim.

Notwithstanding that trustees require adequate time to complete their work ASFA members broadly support the timeframes proposed in the draft Code. The 15 day period for trustees to review an insurer’s intention to decline a claim at section 6.28 has been raised as being particularly problematic and inconsiderate of the activities trustees may need to engage in to obtain further information. It has been raised with us that “this is an important step for the trustee to carefully consider the members’ interests and bona fides of the decision. It should not be rushed to a good practice aspirational time limit. This is likely to compromise decision quality and members will be the loser in that scenario”.

ASFA considers that a sensible remedy to this issue is to extend the circumstances upon which a longer period of review is reasonable. At section 6.29 for example, material could include the trustee determining that further representations or submissions are required, whereas currently the fund member is required to initiate this.

Some of ASFA members have also questioned the requirement in 6.28, relating to declined claims for “all documents obtained during the assessment” to be provided to the claimant. ASFA considers that it would be more practical that the requirement be to provide a list of all such documents and the complete document(s) only at the request of the claimant.

E. Vulnerable consumers

ASFA supports the flagging of vulnerable members but only where the member approves such a record being kept.

ASFA accepts that certain fund members will require more assistance than others due to disabilities, language difficulties and lacking legal identification and hence supports the obligation that the Code places on trustees to put in place policies to assist these members. These policies need to take account of the sensitivity involved in identifying members who require additional or particular types of assistance and their privacy also needs to be respected.

ASFA is of the view that trustees should exercise caution in identifying vulnerable members and should only keep a record of vulnerable status if a member self-identifies that they require particular assistance and are happy for a record to be kept for the particular type of assistance they need. Even then, trustees should be careful about the tone of their communications with the member and the way they adapt their processes and communications to the needs of the member.

F. Premium adjustment mechanisms

In order for funds to retain an opportunity to establish premium adjustment arrangements ASFA supports the proposed transparency and prescribed use of funds measures.

Throughout the ISWG Code development period ASFA has advocated that premium adjustment mechanisms should remain available as arrangements that funds and insurers can enter into. The issues with these arrangements are generally due to a lack of understanding around money flows and the actual use of funds. We consider that the proposals in the Code are required to allow these arrangements to continue, recognising that there are some imperfections as the insured membership base changes over time and funds only (as opposed to insurers as well) are restricted with regards to how funds are spent.

G. Premium refunds

More work needs to be done by the ISWG to codify premium refund protocols, particularly in relation to duplicate income protection claims.

ASFA supports proposals in the draft Code relating to refunding premiums when it is discovered individuals have been paying premiums for cover that they are unable to claim upon, given that in the automatic group insurance environment there will be instances where this arises. While premium refunds are an appropriate mechanism to remedy this, ASFA considers that further work is required by the ISWG to determine when an individual becomes eligible to receive a premium refund as it is unclear how the required notification for such an occurrence arises currently.

H. Staff and independent service providers

ASFA agrees that trustees should bind its third party providers, including insurers and administrators, to obligations of the Code through contractual arrangements over time.

ASFA supports the Code's enhanced training requirements for internal staff and believes this would be supported by enhanced training and accreditation for those who work in insurance provided through a superannuation fund. In the longer term this will involve setting up a broader framework for the necessary knowledge and skills for staff of superannuation trustees who work in the insurance area and determining the content needed for the training to be provided by the relevant Registered Training Organisations.

As to the question of how trustees can ensure their providers comply with the Code ASFA is of the view that third parties such as insurers or administrators can be bound to the Code through incorporating the Code's requirements into their contractual arrangements over time.

I. Code Governance

ASFA considers that trustees will need a degree of flexibility in complying with the Code and supports consideration being given to compliance on an "if not why not" basis.

ASFA considers that of the available options self-regulation is the best in the short term and that other enforcement options can be explored later once there is a track record by which the success of the Code can be judged.

ASFA considers that getting governance of the Code right in a complex environment like the superannuation industry is vital.

ASFA notes that there are a number of considerations relating to governance arrangements which need to be addressed:

- The External Dispute Resolution (EDR) framework and the body assigned the role of dealing with disputes (AFCA) are still in an embryonic and evolving state and much greater certainty will be required before we can contemplate their potential role in Code governance
- Questions have been raised about whether trustees can be legally bound by the Code given their statutory and fiduciary obligations and this needs to be resolved before the various governance options can be assessed.

There are a number of options for Code governance to which we have given preliminary consideration.

One option is an approach in which the industry associations enter into a Memorandum of Understanding to determine who will take responsibility for the various activities associated with the Code.

Another option is for one industry association to own the Code and attempt to bind superannuation funds to it however at this time we do not believe this is likely to be an effective approach.

A further option is the amalgamation of the existing Life Insurance Code of Practice and the draft Insurance in Superannuation Code for trustees. However, the nature of insurance within superannuation is substantially different from that of retail life insurance. It is our view that the very different considerations applying to insurance within superannuation mean that the two Codes should remain separate at least until the new Code has had time to bed down. We acknowledge that the new Code has been constructed to be as closely aligned to the insurers' Code as possible and that administrative synergies should be sought.

With regard to enforcement, ASFA is of the view that options such as voluntary participation/disclosure in the Code should be explored in the first instance while longer term arrangements are looked at. Once the Code is established there will be ongoing opportunities to review its success and effectiveness and the industry could consider further options such as ASIC or AFCA involvement at that time.

ASFA considers that the Code sets a rigorous set of benchmarks for trustees to meet and it must be acknowledged that in certain circumstances trustees will not be able to meet one or more of those benchmarks because of their membership profile. For example: a fund with a high proportion of members in hazardous occupations may not be able to meet the premium cap. For this reason ASFA supports consideration of a flexible approach being adopted for compliance with the Code where compliance is assessed on an "if not – why not" basis.

It is recognised that the administration and monitoring of the Code will also require funding in future. ASFA considers that it would be appropriate to look at options such as funding to be drawn from existing regulator levies.